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COMMUNICATION FROM THE COMMISSION TO THE COUNCIL,
THE EUROPEAN PARLIAMENT AND THE ECSC CONSULTATIVE COMMITTEE

**THE STATE OF THE COMPETITIVENESS
OF THE STEEL INDUSTRY IN THE EU**

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(TEXT WITH EEA RELEVANCE)**

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I. INTRODUCTION

Within the perspective of the new millennium, the European steel industry is increasingly confronted with challenges posed by the globalisation of economies. In its recent Communication "The competitiveness of European enterprises in the face of globalisation"¹, the Commission analysed the competitive position of Europe's industry in this respect. Despite economic turbulence currently characterising some major economies, the EU, by reaping the fruits of the Single Market creation and the introduction of the euro, is succeeding in maintaining a positive non-inflationary growth. However, in view of the further opening of world markets and increased competition, the EU still has an important task of improving its industrial competitiveness, while contributing to the social, economical and environmentally sound development of the EU economy.

The framework in which the EU steel industry operates has changed as a result of the introduction of market-oriented policies (deregulation, privatisation, strict state aid discipline, removal of trade barriers) since the late eighties. Industry operations are, in view of increased public awareness for the environment, pushed towards environmentally "friendly" products and technologies. Moreover, client requirements have induced production of innovative quality products in combination with a high "service" component. For their part, steel employees have obtained improved working conditions, in return for higher qualifications and productivity.

Although the steel business will remain volatile, taking into account, in particular, the new competitors challenging the existing players, the increasing global concentration of client industries, the accelerating technological changes and the permanent cost/price squeeze for steel products, the conditions for facing future challenges are good. This is due to the considerable efforts made by the EU steel industry to reshape its production structure, improve its technological performance and better employ the skills of its human resources. Moreover, via strategic alliances, the industry has transcended national boundaries and developed a truly European production and market base. With the expiry of the ECSC Treaty in 2002, the regulatory framework under which the industry operates will be changed from mainly sector-oriented into the EU policy applied to the whole of the manufacturing industry.

In this context, parties involved in the steel business are challenged to re-assess their strategies in order to identify, in co-operation with national authorities and the Commission, actions necessary to further strengthen the competitiveness of the EU steel industry. This Communication should be supportive in this respect by analysing current key features of the industry (chapter 2), as well as identifying the main challenges in its competitive environment (chapter 3). Actions to be initiated by the industrial actors, Member States and/or the EU Institutions to foster the global and sustainable competitiveness of the EU steel industry, are developed in chapter 4.

2. THE CURRENT KEY FEATURES OF THE STEEL INDUSTRY

2.1. Structure of the EU steel industry

The structure of the European steel industry² has changed considerably following several phases of restructuring and the privatisation of practically all the publicly owned steel companies. Rationalisation of production structures and substantial investments in modern steelmaking processes and technologies has drastically improved performance of steel facilities. Labour productivity has increased substantially, illustrated by the fact that total crude steel output has increased by 20% over the last ten years, whilst the total workforce has been reduced by 40%. The competitiveness of the industry has been further enhanced through cross-border strategic alliances, especially in the field of high value-added steels; or consolidation between one or more former European competitors. Today, over 60% of steel output is produced by 5 groups, against 23% in 1993. At the end of 1998, the steel industry employed about 290 000 people and total production value is estimated at € 75 billion. The EU is both the world's biggest steel producer and the largest single steel market.

Within the sector of first processing, a substantial part of the steel industry's output is manufactured according to different user requirements. This sector is composed of various industrial branches, in particular pipe and tube makers and various companies engaged in cold rolling and drawing. Together these branches count some 3000 firms, many of which are SMEs, employing more than 150.000 workers and representing an annual production value estimated at over half of that of the ECSC Steel industry. Moreover, another group of companies, many of them being world leaders in their field, offer their services to the steel industry and its clients. Apart from the suppliers of steel processing installations, other equipment and consumables and a vast range of professional services, this also includes steel service centres and/or steel stockholders and scrap recovery and recycling companies.

2.2. Technology base

Steel is produced by two different basic technologies. Integrated steelworks produce crude steel out of iron ore and coal. Due to the high quality of steel made, this technology accounts for most of the production of flat sheets and plates. The Electric Arc Furnace (EAF), which requires a lower capital intensity and provides a greater operational flexibility, was in the past primarily aimed at long products (including special steel products). Driven by new technological developments, it has started to be used also for flat steel production. This requires generally high quality scrap or the addition of "virgin" materials like sponge iron (DRI), hot briquetted iron (HBI), cold pig iron or hot metal from blast furnaces or smelting reduction plants. Currently the part of steel produced by the EAF route amounts to 37% in the EU, which is comparable to the situation in Japan, against 45% in the USA.

Technological developments, aiming at improvement of processes and products, as well as the reduction of raw material and energy consumption, have become continuous, with the time horizon for selecting, implementing and amortising investments in new technology significantly compressed. Moreover, the results of RTD are rapidly becoming available on the market, also offering competitors the possibility of obtaining state of the art technology.

In order to keep a competitive edge on technology and to achieve financial returns from it, the EU industry strongly depends on its ability to innovate. This continues to be addressed through RTD programmes at company level and through co-operative research fostered and supported under the ECSC Treaty and through the progressive inclusion of steel research in the 5th Framework Programme of Community RTD³.

2.3. Customer base

Steel is an essential input for the whole of economic activity, and is consumed in both the investment goods industry (construction, machinery, heavy transport) and in the consumer goods industry (automotive, household appliances, packaging). The EU steel industry has been particularly successful, through close co-operation with its clients, in the field of innovation aiming at improving product standards and properties (e.g. elasticity, tolerances, weight and corrosion resistance). The range of steels is constantly extended towards new applications and high value-added special steels, to supplement the existing range of so-called ordinary steels. As a result, not only the competitive position of steel compared to its potential substitutes like aluminium, plastic and cement is re-enforced but these materials are also increasingly used to complement each other.

In this respect, it is important to note that the EU steel industry has contributed to the global competitiveness of a wide diversity of metal-based sectors of which three (transport, machinery and fabricated metal products) are ranked in the top 5 sectors according to export shares⁴ of the EU industry.

In order to meet different customer requirements, a variety of commercial relationships have been developed. Key clients, like the automotive industry, are for the most part directly supplied by the industry on the basis of (mostly one year) contracts. Moreover, indirect sales on the basis of short-term contracts and spot basis take place via stockholders and service centres, encompassing about 40% of steel production intended for the EU market. Although information and communication technologies (electronic commerce, etc.) are increasingly used to facilitate trading relations and organisation structures, the limits of ICT utilisation has not yet been fully exploited in the steel business.

2.4. Material base, energy and transport

The integrated steel industry in the EU depends on a substantial part of its raw materials (e.g. iron ore and coking coal) from overseas markets. Due to the relative abundance of these materials no major supply bottlenecks are expected. EU steel companies are therefore less involved, compared especially with Asian steel producers, in upstream mining investments. Moreover, improvement of environmental performances can be achieved through co-operation between the EU steel industry and the suppliers of iron ore, as well as in the preparation of coking coal.

Ferrous scrap is the principal raw material for electric steelmaking. Availability of scrap is related to levels of economic development and the EU is a large collector of scrap and still a net-exporter. Due to the high impact of transport costs on the scrap trade, regional markets are largely developed, for example between the CEECs and the EU. In order to obtain better qualities of scrap, initiatives are being taken to improve its collection and recycling. The latter is not only an environmental priority, but is also intrinsically profitable thanks to energy savings and economies in materials.

In order to extend their raw materials base, and following the drive towards higher value-added products, electric steel producers increasingly combine scrap with DRI/HBI and/or other virgin iron.

A further group of raw materials, essential for the production of special steels, are ferro-alloys. These materials are for the biggest part imported and constitute an important and increasing part of production costs. Long-term supply has to be secured through facilitating market access and increased competition between suppliers.

Electricity and natural gas make up a significant part of steel production costs. Within the EU, electricity and natural gas prices show important differences, in part because of taxation but also because of different structures and regulation of the supply industries. Regulatory regimes can and do lead to disparities between Member States, especially for electricity charged to the steel industry. Effective implementation of the Directives on electricity and gas markets should ensure further convergence of price levels.

The steel sector is very transport intensive. To illustrate this, after crude oil, iron ore and coal are the most important commodities in the world's sea-borne trade. Moreover, almost 30% of all finished steel products are crossing borders world-wide. Depending upon the quality of the steel product, the distance to be covered and the transport means to be employed, transport constitutes between 5 and 15% of the selling price. Several initiatives have been carried out by the Commission in the field of transport, focussed for example on the improvement of the functioning of the Single Market, particularly through the harmonisation of technical standards and broadening the external dimension by improving transport links between the EU and third countries. However, an improved and more harmonised regulatory and competitive framework for rail freight, important for transporting bulk materials, still needs to be achieved for both economic and environmental reasons.

2.5. Human resources

The traditional image of the steel industry as a large-scale employer has been substantially eroded, having lost almost 70% of the workforce it had in 1975. In order to support the need to reduce production costs, employee redundancies have been accompanied by an extensive set of social measures. Today, the steelmaker's objective can be summarised as "achieving the most cost-effective production and selling of high-quality products with the smallest possible highly skilled, committed and integrated workforce"⁵. Consequently, efficient human resources strategies are critical to strengthening the competitiveness of the steel industry. The trend towards the "empowerment" of employees so that they can do the best job for their enterprises, and the introduction of profit centres and simultaneous engineering next to "gain-sharing" and permanent training, are part of these strategies.

2.6. Financial performance and cost structures

Since the end of the last restructuring phase, the financial performance of the EU steel industry, especially in comparison to its competitors in the TRIAD (EU, US, Japan), has significantly improved. Operating costs have been reduced through the introduction of advanced technologies, efficiency and rationalisation measures and employment reduction. As a result, manpower productivity in the EU industry is amongst the highest achieved in the steel business.

Although further cost reduction will be actively sought, future cost flexibility risks to be limited especially because employment costs (including the non-wage element) in the EU remain high compared to most competitors.

In this respect, it is important to note that the EU steel industry faces competitors benefiting from comparative cost advantages (labour, energy, taxation), like the CEEC, and/or those confronted with less stringent regulations (state aid, environment etc.).

Moreover, as has been observed in the case of Asian companies improving their export position following devaluation of their home currencies, cost competitiveness is strongly influenced by exchange rate fluctuations. Being cost competitive is all the more important because, to a certain extent, steel products can be labelled as homogeneous, resulting for individual producers in a highly elastic relation between steel demand and prices. Furthermore, price transparency for ordinary steel products and special products with standard dimensions, is almost perfect because of regular publications of market prices by specialised agencies (available on the Internet).

These factors, in relation to falling demand in Asia, have induced heavy price volatility throughout the second half of 1998. Sustained low price levels do not allow the steel industry to capitalise on the fruits of its efficiency efforts, nor do they contribute to the funding of new investments and RTD. In order to reduce the impact of sheer price competition characterising the trade in ordinary steels, the EU industry is increasingly focusing on the production of steel products, and the provision of related services, tailor-made to the needs of those (key) clients that are prepared to pay a "quality" premium.

2.7. Capital and investments

Following privatisation and the expansion of the share of private shareholders in their capital structure, the EU steel industry has been able to reduce, more successfully than US and Japanese steel producers, their debt position in favour of equity. Achieving a balance between shareholder value creation and the need for the industry to have a steady flow of capital at its disposal, in relation to the relatively long time span necessary to achieve profits on new investments, is not easily met if shareholders are merely interested in short-term gains. This can be illustrated by the sharp fall in share prices of several steel companies in the second half of 1998, triggered by the fear that the global steel market is entering into a new crisis. However, since the beginning of 1999 share prices of most EU steel companies have started to recover. What should count for companies concerned, moreover, is the capacity to continue to provide long-term satisfactory financial returns.

In order to improve competitiveness, the EU industry has no other choice but to permanently upgrade existing facilities and to invest in new technologies requiring substantial investment levels. The investment potential is directly related to profit levels and the overall cost of capital. Factors that influence the cost of capital are particularly interest rates, taxation and debt/equity levels. The ongoing integration of European financial markets, associated with the introduction of the Euro, offers important advantages for industry. The increased size of the capital market and the sharper competition between financial intermediaries should help to reduce the cost of capital. In addition, capital cost will be reduced because hedging cost disappears in the absence of currency risks within the eurozone. In comparison to some of its competitors (i.e. Japan), however, cost of capital remains higher for EU firms.

3. THE MAIN CHALLENGES TO A GLOBAL AND SUSTAINABLE COMPETITIVENESS

3.1. The growing impact of globalisation

Important steel customers, like the automotive and mechanical engineering industries are increasingly investing in, and consolidating with, companies outside the EU. Reasons to do so are to produce in closer proximity to end-users, to search for cost savings, to avoid barriers to trade, and to improve servicing capabilities. Global positioning and concentration of steel customers result in increased market power, stricter product requirements and standardisation, as well as the need for sophisticated delivery and logistic systems. As far as participation in foreign production plants are concerned, EU steel producers have a considerably lower degree of investments in regions like the Americas and mainland Asia than, for example, Japanese firms⁶.

The trend towards further liberalisation of international steel trade, and thus increased international competition, has manifested itself clearly. For their part, most OECD countries committed themselves, during the Uruguay Round, to completely abolish their tariffs on steel imports by the year 2004. Furthermore, important steel producers like Russia, Ukraine and China would be expected to subscribe to WTO commitments upon their eventual accession to the WTO.

The financial and economic crises in SE Asia, Russia and parts of Latin America have seriously disturbed traditional international trade flows. In response to the pressures on their markets, steel industries in various parts of the world have increasingly sought protection through anti-dumping and anti-subsidy measures, as well as through other means, such as tariff increases or minimum import prices.

In the US, the Administration has come under intense pressure from industry and Congress to stem imports following a spectacular increase thereof in 1998. The US steel industry has presented a wave of anti-dumping, anti-subsidy and safeguard (Section 201) complaints. Congress has launched a series of bills containing provisions, some of which appear to be at variance with WTO trade rules, such as the Emergency Steel Loan Guarantee Act of 1999. Finally, the Administration has presented on 5 August 1999, a New Steel Action Plan which proposes, a strengthening of the US trade laws, a global conference on over-capacity and a surveillance of the US steel imports, which could act as an early warning system. The Action Plan gives the impression that across bilateral consultations some disguised Voluntary Restraint Agreements (VRA) with the major steel exporting countries to the US are not excluded.

Since the collapse of negotiations towards a multilateral steel agreement, the OECD Steel Committee has remained the only international forum for dialogue on steel. The EU has been instrumental in guiding the Committee towards a more effective role in relation to trade and trade-related issues.

In 1997, on an EU initiative, the Steel Committee launched a "peer review" of trade and trade-related policies, to increase transparency and debate on issues such as tariff and non-tariff market access barriers, dumping and subsidies. The EU has provided a comprehensive "country report", but the exercise has been delayed because some other country reports have been incomplete, notably with respect to state aid granted at sub-national level.

In November 1998, again following an EU initiative, the Steel Committee issued a statement on the need to maintain open markets in response to the international steel trade crisis. The EU is monitoring the actions of other countries to ensure that they respect the principles established in the Steel Committee statement. The Steel Committee should enable the EU to address crises, such as the present trade situation, in close consultation with its partners, and to influence trade policy developments through peer pressure.

3.2. Matching steel supply and demand

Past experience shows that crises in the steel industry usually have their roots in imbalances caused by rapid demand fluctuations in combination with rather rigid supply structures and global over-capacity, often provoked by subsidised investments and/or public support of non-viable companies. The immediate cause of the recent steel trade problems, can be traced to the collapse of demand for steel in SE Asia and currency realignments increasing the short-term competitiveness of crisis-affected countries.

Fluctuations in demand are related to business cycles but also have structural backgrounds. Economic cycles influence steel demand to a large extent, bearing in mind that steel is used for both consumer and capital goods. Structural factors stem from changes in customer preferences, product and process innovation, as well as substitution of steel by other materials and vice-versa. In terms of volume, steel demand is expected to increase more outside mature steel-markets like the EU, Japan and the US, especially in favour of Asian and Latin American countries. The principal reason for this is the potential demand for steel products, particularly for infrastructure upgrading. From a quality perspective, however, the industry expects an important potential for increased steel demand in highly developed countries (durable consumer products, capital goods) as a result of further product development.

As regards steel production, the UN Economic Commission for Europe (UN/ECE), warned in 1997 of a potential over-capacity as a result of the rapid build-up of new steel-making capacity in several net-importing regions (e.g. North America and Asia). Despite the fact that in the meantime a number of ambitious projects have been suspended or cancelled due to the recent turbulence on steel markets, total finished steel capacity will nevertheless continue to expand. Although the volume of world steel trade has declined lately, particularly because of lower demand in Asian economies, experts forecast a recovery in a few years time, on condition that benefits of trade liberalisation are maintained, and escalation of trade conflicts is avoided. In accordance with the above-mentioned trends, it is expected that world steel trade will focus increasingly on higher value-added products at the expense of ordinary steels, being increasingly traded on a regional base.

This is due to the expected build-up in steel capacity, but also to the fact that the production of special steels is to a great extent concentrated in advanced steel-producing countries.

In 1998, the EU steel industry recorded a steel trade deficit (in volume) with the rest of the world for the first time in its history, resulting from an exceptional surge in imports of around 50% and a fall in exports of around 13%. In value terms, the EU remained a net exporter, owing to both low-priced imports and the fact that EU exports consist in general of higher value-added products, but the trade surplus shrank by a third.

In the second quarter of 1999, a gradual recovery of price levels as well as a decrease in imports in the EU market have been observed. However, the situation remains rather fragile and can be easily disturbed by any other economic downturn in the international market. Moreover, long-term viability of EU steel companies will also depend on the extent to which major steel users influence the adaptation of the steel industry through their purchasing strategies. This is already starting to happen in the automobile industry. A major carmaker recently announced a multi-annual, global strategy to purchase steel from around 40 suppliers. If major steel consumers in the EU maintain production capacities in the EU, and if EU steel producers are successful in competing with imports, the EU steel industry will remain in a good position to optimise the mix between deliveries to the internal market and exports to third country markets. If, on the other hand, major steel users re-locate part of their production outside the EU, the need to export and/or to follow these clients, via increased industrial participation outside the EU, will have to become an important factor in strategic decision-taking by the EU steel industry.

3.3. The EU enlargement

The objective of the enlargement process is to improve the viability prospects of the industry in the candidate countries, in order to cope with the competitive pressure arising of full EU-membership. The Europe Agreements concluded with the associated Central and Eastern European countries, provide for trade without any restrictions and with zero duty in respect of steel exports to the EU. The associated countries are progressively dismantling tariffs (this should end on 31 December 1999), while the EU has done so already. The Europe Agreements contain a Protocol on ECSC products (Protocol 2), which includes provisions on public aid for restructuring. The five-year "grace period" on state aid has expired for most CEEC and a further five-year extension has been requested. The conditions for such an extension (sound national restructuring programme and viability plans for the individual companies), must be met by the countries concerned before extension is granted. The Commission will monitor strictly these conditions, especially in view of the delay in the privatisation and restructuring process in most of the CEEC, which will increase the risk of granting non-compatible state aid to the steel industry.

The industry in candidate countries presents several strengths, such as relatively low labour cost and a good level of technical qualification of the workforce in a number of sectors, like steel and mechanical production. Weaknesses, on the other hand, include: outdated production set-up in combination with slow implementation of modern production techniques, low energy efficiency and overstaffing. This results in sub-optimal productivity levels and product standards in need of further development, as well as in environmental constraints.

Priorities for industrial policies in candidate countries include privatisation, investments in human and physical capital, increased productivity and product quality, as well as the creation of job opportunities as an alternative to those lost in the steel business. The parallel implementation of these priorities is advancing too slowly and many steel companies are facing financial difficulties.

Opportunities for the EU industry are open access to potential growth markets and possibilities for industrial specialisation, based on comparative advantages offered by the CEEC. However, thorough restructuring in these countries is a basic condition for the participation of EU and other private investors. If this is achieved, entrepreneurs from the CEEC and the EU will mutually benefit from the larger European market.

Moreover, successful integration of the CEEC steel industry, representing a major economic force in the candidate countries, will constitute a major impulse to overall economic integration.

3.4. The changing EU regulatory framework

In order to prepare the steel industry to the expiry of the ECSC Treaty in 2002 and accompany its integration into the EC Treaty, a phasing-out/phasing-in policy has been developed. As far as budgetary matters are concerned (restructuring and social support, loans etc.), this process started in 1992. Phasing-in has proven to be difficult as far as RTD is concerned, due to the fact that EC based RTD (Framework Programmes) is less oriented towards the specific needs felt by the industry compared to ECSC-financed RTD. During the Amsterdam Summit, a resolution was adopted to assure continuation of RTD activities, in line with the needs of both the steel and coal industry, by employing the financial reserves of the ECSC. The Commission has submitted to the Council, at the latter's request, a Communication containing suggestions to implement this resolution⁷. On the basis of this Communication, the Council has adopted in April 1999 new resolutions⁸ to be legally implemented in due time.

The Single Market provides firms in the EU with the advantage of acquiring trans-frontier experience and exploiting scale economies. This framework can provide leverage for improving access to global markets. However, in the 1998 business survey organised by the Commission, companies identified a considerable range of trade barriers (compatibility with different national specifications; testing, certification or approval procedures; public procurement, taxation and state aid practices) which continue to prevent them from realising the full benefits of the Single Market. Next to reducing the impact of trade barriers, EU steel companies would be able to benefit more from the effect of free competition if further liberalisation is achieved in sectors (e.g. financial services, transport, electricity and gas) providing essential inputs to the industry.

As far as environmental policies are concerned, various instruments are being considered, nationally and at the EU level, in order to implement commitments according to the Kyoto Protocol of the United Nations Framework Convention on Climate Change (UNFCCC). These concern voluntary or negotiated Environmental Agreements⁹, carbon-energy tax, the Kyoto Protocol's flexible mechanisms and Integrated Pollution Prevention and Control (IPPC).

The IPPC Directive lays down measures designed to prevent or reduce emissions in air, water and land including measures concerning waste. Permits will be granted by local authorities in Member States, that will determine in each case the Emission Limits Values to be set. In this context, the European IPPC Bureau has been entrusted with the responsibility to write reference documents (BREFs) describing the Best Available Techniques (BAT) on the basis of an information exchange between Member States and the industries concerned. The BREF on iron and steel production, which has recently been finalised, identifies the reduction of air emissions and the management of solid waste as key environmental issues for the sector.

4. ACTIONS TO ENHANCE A SUSTAINABLE COMPETITIVENESS WITHIN A GLOBAL PERSPECTIVE

4.1. Reinforcing the human and technological bases for a more innovating steel industry

In the Communication "The competitiveness of European enterprises in the face of globalisation", the Commission has stressed the need to develop an enterprise culture and risk-taking spirit that stimulate companies to go "global". Recommendations concentrate on the need to review learning systems (i.e. technical competencies, ICT-skills, spirit of enterprise), and the necessity to improve the efficiency of research and the exploitation thereof (including the protection of intellectual property and access to risk capital for innovative technology). To support this process, public funding should be reoriented to non-material investments. The objective is to contribute to the modernisation of the industry and its capacity to adjust to evolving customer requirements, through combined effects of improved industrial capability and innovation capacity. To this end, opportunities are available to the steel industry under research training programmes included in the 5th RTD Framework Programme. These points will be developed below, taking into account the steel industry's particular characteristics, in order to identify the most adequate set of actions to be taken by the main actors in this field.

4.1.1. Developing human capital

Skill and knowledge requirements have risen continuously, not only including knowledge of technical processes, but also the ability for analysis and an aptitude for teamwork. Related to this, is the rapidly changing world of work, driven by computerisation and information technologies¹⁰. A continuous training process and the establishment of "best practice" education and training arrangements are necessary to adapt skills to these changes. Moreover, new technologies will influence the organisation of work thereby promoting "self management" of production teams and lesser levels of hierarchy.

The aim of further developing the human capital is to facilitate the integration of new forms of work organisation techniques into the productive process and to improve performance of production systems, thereby stressing socio-economic aspects i.e. employment, health, safety and job satisfaction. Currently, the steel industry gives way to an exchange of "good practices" on these matters through regular meetings between human resources Directors.

As far as new staff is concerned, the modern steel industry does not require a mono-thematic specialisation, but a solid technical and scientific base. To attract highly qualified staff, the steel industry is committed to intensify its contacts with universities and, in general, further work on its image (safety, durability and environmental performances in relation to high-technology).

4.1.2. Extending the social dialogue

An essential task is the need to motivate people through effective participation and responsibility sharing in the decision-taking process, in order to achieve the best results both in quality and quantity of production as well as in response and service to the client.

The management of the EU steel companies and the national and EU-wide Federations, as well as the steelworkers' trade Unions, are determined to deepen their long existing social dialogue. Joint identification and implementation of actions will further reinforce the quality of the human assets of the industry, being one of its more evident competitive advantages in relation with third countries. In this respect, activities of the "Mixed Steel Committee" but also the programme "Management of Change and Human Resources", undertaken by the industry with the support of the Commission, are good examples.

A recent Communication¹¹ of the Commission aims to promote social dialogue at European level. The current structure of the "Mixed Steel Committee" could be replaced, after the end of the ECSC Treaty, by a sectorial dialogue that would be the forum for the exchange of information on best practices, and for the negotiation of agreements reconciling the companies' need for flexibility and job security for the employees.

4.1.3. Technology, innovation and RTD

Technological innovation is one of the key factors for the orientation of actions and policies in the steel sector. Three driving forces are in play: the need to produce new products to satisfy customer requirements, the need to reduce production costs by new production technology and the need for clean technology (including more recycling).

The key factor for moving in this direction is closer co-operation with user sectors in the field of co-operative applied research. Consequently, the process of improving product requirements and standards, bearing in mind environmental constraints, fed through a continuous process based on close co-operation with key customers (i.e. user-driven) has to be broadened and reinforced. In this respect, it is judged very positive that an ambitious project like the UltraLight Steel Body (ULSAB), but also projects focusing on innovative and durable building materials and steel packaging, have had a favourable impact on co-operation between steel producers, manufacturers, clients, researchers and designers. These experiences can be used as models for other steel consuming sectors.

In addition to the development of new products, research is focused on a more efficient use of raw materials, optimising energy consumption, reducing polluting emissions and decreasing investment and operating costs. This research is being speeded up, and the industrial implementation of new technologies (e.g. smelting reduction processes, DRI, compact strip mill, Near Net Shape Casting) throughout the production process, will mark the beginning of the millennium. Clear actions need to be developed for RTD to be sustained bearing in mind that EU companies devote a smaller part of their resources to RTD compared to key-competitors.

Consequently companies must strengthen their efforts in this direction. Member States should also reinforce national research structures (universities, RTD centres). Community institutions, for their part, are currently carrying out two actions. Firstly, the phasing-in of steel research to the 5th Framework Programme. Secondly, the Commission has prepared a Communication putting forward principles, which have been recently agreed upon by the Council in order to organise after 2002 the financing of complementary research from the ECSC reserves.

In the field of Electronic Commerce, both the steel business and the Commission (e.g. the "Electronic Commerce Open Market Place for Industry Sectors" initiative) are actively promoting its application within the industry thereby giving special attention to the specific needs of SMEs.

4.2. Ensuring a level playing field within the EU and globally

4.2.1. Reinforce the benefits of the Single Market

European companies' access to world markets will be facilitated if additional benefits can be obtained from effective competition within the Single Market. In this respect the Single Market and the single currency are key elements of Europe's response to the globalisation process.

Much of the Single Market action plan has been successfully implemented. However, despite this progress (as mentioned in chapter 3.4), the Single Market is still not operating optimally¹². Increasing price transparency and facilitated cross-border transactions brought about by the Euro, while serving as a powerful integrating force, will also bring into focus the areas where problems remain. The Commission has prepared an overview of actions included in the Action Plan¹³ for the Single Market, which still need to be completed. As far as the steel industry is concerned, speedy follow-up is essential in the harmonisation of standards (for example on construction products) and the extension of SLIM (modernisation CN and HS). The effective implementation of the Directives on electricity and gas and the liberalisation of transport markets are other priority actions.

4.2.2. Phasing-out/phasing-in of the ECSC Treaty

Actions related to the expiry of the ECSC Treaty in 2002, on top of those mentioned in paragraph 4.1.3 (RTD), can be summarised as follows:

- Phase-out the ECSC statistical framework by reducing the frequency of reports and breakdown by Member States until 2002. After 2002, ECSC statistics are to be harmonised in line with the general statistical framework. Commission services are preparing, in co-operation with the steel and other basic industries and Member States, a feasibility study that will concentrate on legal aspects, and the transitional measures needed to improve the industrial statistics in the EU after 2002. The steel industry may develop an information system tailor made to its specific needs, in full respect of the competition rules in this field.
- Reduce the frequency of the "Forward Programme for Steel", to be adopted on a yearly basis as from the year 2000 on.

- The rules affecting trade in ECSC steel products are to be fully integrated into the Common Commercial Policy governing EC products.
- ECSC Decisions related to steel pricing policy, will be phased out by reducing the obligation of producers to submit less relevant prices and volumes information.
- The legal framework for concentrations in the steel industry will be aligned with the regulations in place for all other industrial sectors¹⁴.
- A new "Steel Aid Code" in the form of Commission guidelines based on Article 88 (1) of the EC Treaty is currently being prepared by the Commission. These rules, to be applied for a sufficient period, should be based on the approach adopted in the existing aid code.

4.2.3. Competition policy and state aid

Developing and administering a "workable" competition policy is one of the most important government activities in supporting the competitiveness of industries, both in home and export markets. For the steel industry, with its relatively homogeneous products and large number of suppliers, free and fair competition constitutes an essential element in securing a future. There are three aspects of competition policy particularly important in this context: the treatment of horizontal and vertical agreements, mergers and state aid:

- Horizontal co-operation in the field of RTD already receives a favourable treatment from the competition policy's point of view. A swifter and simplified treatment is still needed for those cases involving such agreements, in so far as they do not create distortions of competition and they stimulate EU companies to close the gap in terms of international technology alliances. Regulations on vertical agreements are already being reviewed, in order to take into account intensified contacts between companies all over the world not in the least driven by the progress in information and communication technologies.
- It is expected that the near future will bring an increasing amount of consolidations world-wide in the steel industry, mainly through mergers, take-overs and joint ventures. The steel industry still is, for a big part of its products, less concentrated than other basic industries, whereas the demand side becomes increasingly concentrated.
- The Commission reports prepared at the request of the Cardiff European Council of June 1998 recommend that Member States should set precise objectives for a reduction in state aid and redirect them away from ad-hoc and sectorial aid towards measures designed to correct market distortions. In the meantime, it is important that strict rules are maintained so as to avoid distortion of competition among EU steel producers, even after the expiry of the ECSC Treaty in July 2002 (see 4.2.2). These rules would also apply in the CEEC steel restructuring process. Other steel-producing countries should also be encouraged to apply strict state aid disciplines, bearing in mind world-wide over-capacities and substantial Government involvement in the steel sector of some third countries.

The new round of WTO negotiations provides an opportunity to develop a multilateral framework of competition rules. As business activities become increasingly global in nature it is essential that WTO members be committed to the adoption and effective enforcement of a competition law regime and to enhanced co-operation in order to deal with anti-competitive practices affecting international trade and investment.

The EU has taken the initiative to launch discussions on this subject in the WTO, which has established a working group to consider the inter-action between trade and competition policy.

As regards the global approach to subsidisation, all WTO Members are bound by the WTO Agreement on Subsidies and Countervailing Measures ("SCM Agreement"). This agreement which sets out a comprehensive system of subsidies disciplines - explained immediately below - applies to all economic sectors including the steel sector. The main feature of the SCM Agreement, as opposed to internal EC State aid rules for steel, is that subsidies are allowed with the exception of two types of prohibited subsidies ("red" subsidies), but are always subject to remedial action if adverse economic effects are caused to the industry of other WTO Members unless they fall into the special "green-light" category. In particular, the SCM Agreement prohibits export subsidies and import substitution subsidies, but grants non-actionable status to subsidies which are non-specific and to certain specific "green-light" subsidies (RTD, environmental and regional aid). All other subsidies are permitted but subject to dispute settlement or CVD action by other WTO Members if they cause adverse effects. Certain "dark amber" subsidies (subsidies exceeding 5%, coverage of operating losses and debt forgiveness) are presumed to cause such effects; this presumption is rebuttable by the subsidising country and specifically does not apply to the one-time rescue or restructuring aid allowed under Community state aid rules. The "dark amber" and "green-light" provisions, contained in Articles 6.1 and 8 of the SCM Agreement, are due to expire by the end of 1999, unless they are renewed by WTO Members.

Given the existing multilateral subsidy framework, the failure of past efforts to reach agreement on steel-specific subsidy rules and the absence of sectorial initiatives in the New Round, the best chance of creating a level playing field on subsidies at the global level would be to make full use of the provisions in the SCM Agreement and if possible to re-enforce these horizontal subsidy disciplines in the New Round of WTO negotiations. In addition, the EU will continue to press for greater transparency on the trade, competition and state aid policies of other countries with respect to steel restructuring processes in the OECD Steel Committee.

When negotiating bilateral trade and co-operation agreements with third countries, the Commission seeks approximation of competition and state aid disciplines with a view to reducing distortion of trade and industrial competitiveness. Where appropriate, the Commission also negotiates specific competition and state aid commitments on ECSC steel products, including conditions relating to the use of state aid for restructuring. This is already the case for the EU's agreements with countries in Central and Eastern Europe, Turkey, Russia, Ukraine and Kazakhstan. The latter should enter into force on 1 January 2000.

In future bilateral negotiations with major steel producing countries closely associated with the Community, the Commission will seek to promote strict disciplines on competition, state aid and restructuring. In so doing, it will take account of the provisions contained in the EU's internal legislation and the Guidelines adopted in the Industry Council of 16 November 1998. These Guidelines recommend that countries currently undertaking steel industry restructuring and especially those with important Government involvement in this process should prepare a comprehensive restructuring programme which should include, inter-alia, a demonstration of how strict compliance with relevant state aid rules will be achieved or full details of the amount, nature and duration of the state aid proposed, realistic and comprehensive viability plans for the individual companies and strict timetable for the restructuring measures, including capacity reductions and a detailed monitoring of the progress in implementing these measures.

It is important to remember that Community industry will have recourse to countervailing or WTO dispute settlement measures against all third countries until implementing rules on state aid are properly applied. It goes without saying that such measures will be available with regard to all third countries where no bilateral arrangements on steel aid are envisaged.

4.2.4. Access to global markets

Markets throughout the world are increasingly open for foreign competition. However, exporters are still too often faced with an array of trade barriers, ranging from prohibitive high customs tariffs, import restrictions, as well as bureaucratic regulations (licensing, certification, inspections etc.).

On tariffs, the EU and certain other WTO partners committed themselves in the Uruguay Round to eliminate tariffs on certain steel products by January 2004. In the New Round, the EU will be encouraging other countries to accept the same commitment. It will also be seeking substantial tariff reductions on all products, increased tariff harmonisation (for example through tariff bands) and 100% tariff binding.

Trade barriers are often related to national standards applied by a number of steel importing countries. These standards need to be made more transparent and harmonised to those internationally agreed upon (e.g. European Standards). Moreover, a common basis for an international trade law (following for example the UNCITRAL initiative) should be developed to protect firms from malpractice by trading partners, often covered by national legislation.

Companies in the steel business are called upon to make use of the Market Access Strategy launched by the EU¹⁵ in order to inform the Commission about trade barriers so that the Commission can seek to eradicate barriers that are incompatible with a third country's WTO or other international commitments.

4.2.5. Actions to reduce the environmental impact of steel operations

The development and implementation of environmental, economic and social policies, including the definition and evaluation of their instruments, should take into account the inter-relationship between these policies and the potential impact thereof for the competitiveness of the Community's industry. Targets adopted within the Kyoto Protocol on greenhouse gas emissions reach far beyond the environmental background and have a truly global dimension. The EU steel industry has already contributed to the objective of the UNFCCC as it has for the past 20 years reduced the amount of greenhouse gas emissions by almost 40%.

The industry is evaluating the possibility of voluntary or negotiated Environmental Agreements, considered as an environmentally efficient and cost effective way to achieve reduction targets. The Commission will study any proposal from the steel industry on the possibility to employ such agreements at European level. These agreements could play an important role as part of the policy package required by the Kyoto Protocol. The Protocol is asking parties to demonstrate progress in reducing their emissions by 2005 in view of the first commitment period of 2008 – 2012.

Meanwhile, because of the investment time span in the steel sector and the actual limits on improvement with existing technologies, the EU steel industry considers that reduction targets should be dealt with over a longer period.

The fact that the sector will be subject to the provisions of the IPPC Directive will contribute significantly to limitation of carbon dioxide emissions, because it will ensure that industry operations will move in the direction of Best Available Techniques (BAT). The Commission has launched, with the involvement of governments and industry, the information exchange on BAT as a useful instrument for identifying the extent of possible improvements and technologies capable of achieving them. This exercise must continue and give rise to concrete actions in the Member States.

A major characteristic of steel is the fact that it can be recycled, with the double advantage of cleaning up the environment and using the latent energy content of scrap. The demand for high quality steel products implies that cleaner scrap is required. In order to meet this demand, operators in the recycling chain have to adjust their operations. In this respect, recommendations presented in a recent Commission Communication¹⁶ should be given a speedy follow-up, especially in relation with the review of the waste definition and with the harmonised implementation of waste management legislation.

4.3. Promoting industrial co-operation with third countries

4.3.1. Central and Eastern European countries

In order to support the enlargement process, the Commission has adopted in 1998 a Communication entitled "A global approach to promote regional and social conversion and to facilitate industrial restructuring in the CEEC: the case of steel"¹⁷. The objective of this Communication is to contribute to the adjustment of the steel industry in the CEEC, in view of their integration into the Single Market. The measures proposed should act as a catalyst for co-operation between the private sector, social partners, the administrations of the countries concerned and the International Financial Institutions (EIB, EBRD, WB etc.).

As stipulated in the aforementioned Communication, Member States and the Commission, with pre-accession financial assistance (e.g. PHARE and the new Instrument for Structural Policies for Pre-accession), should assist in the funding of accompanying social and regional measures of the steel restructuring process, support efforts to remove legal and administrative obstacles to investment, and provide expert assistance in fields such as market research, the establishment of business plans and the preparation of privatisation. Moreover, Member States and the Commission will continue initiatives to promote a dialogue between all governments involved, in the framework of the European Steel Forums, of which the first edition took place in October 1998 and the second one is scheduled for March 2000.

Participation of EU firms, for example in the privatisation of CEEC steelworks, taking part in specific steel operations or through creation of joint ventures to develop specific steel applications, are effective ways to stimulate a speedy and efficient restructuring of the steel industry. This may also include implementation of joint RTD projects. Producer associations have to play a major role in this respect.

Furthermore, labour unions and other stakeholders should play a role by organising meetings with their counterparts in the CEEC and explain their respective roles in a modern market economy. Involvement of social partners in this process is particularly important, as it is supportive in the creation of a level playing field for private initiatives. These initiatives will enable the CEEC industry to prepare itself for the challenges of accession to the EU and, more generally, for the increasing globalisation of steel markets.

CEEC governments have to create appropriate conditions to achieve a level playing field, before accession takes place, as noted in the aforementioned Communication. Most important in this context is the elaboration and adoption of a sound and comprehensive steel restructuring programme, based upon the viability of individual steelworks, with a clear timetable for the implementation thereof.

4.3.2. Industrial co-operation with other countries

The Commission and steel business have to develop actions to reduce the risks and to take the opportunities that globalisation offers in relation to other (potentially) interesting third markets. Commission services will therefore closely monitor developments in these markets, in order to foster the creation of level playing fields for investments. One way to do so is to address (in Contact Groups, Round Tables etc.) issues like industrial co-operation as well as problems encountered by EU companies on third country markets. On-going activities in this field are the EU-Russia Round Table, the MEBF and the TABD, whilst the ASEAN, South Africa and China are earmarked as future activities.

These initiatives should, however, not be limited to a mutual exchange of information, although useful in itself, but should lead to tangible results such as MRAs, codes of good conduct, creating safe conditions for investments, limitations of "buy-local" rules etc. Other initiatives include the organisation of steel conferences as well as different types of workshops focusing on specific problems facing the steel companies in certain countries, such as adoption of environmental regulations. Moreover, recent initiatives such as the Mercosur steel conference and different workshops in the CEEC proved to be successful in fostering contacts between different stakeholders.

In order to improve the effectiveness of these initiatives, close co-operation is needed between public authorities, both from the Union and third countries involved, and the respective industry participants. The latter should not be limited to producers and their associations, but should also include other market operators like steel consumers, steel stockholders/service centres, as well as representatives of labour unions.

4.4. Improving co-operation between main stakeholders

Challenges facing the EU steel industry have an impact on all firms within the steel business, whether it concerns the biggest steel producer or small recycling firms. Moreover, although a relatively high degree of integration exists throughout the production chain, factors that affect the competitiveness of individual companies are not necessarily the same. Consequently, initiatives to improve competitiveness, for example by means of strategic partnerships, should be based upon a detailed analysis of the specific competitive factors of the individual stakeholders.

In this respect it is important to note several initiatives by Member States and the Commission to further develop the EU benchmarking initiative, especially as it focuses on framework conditions, i.e. factors that are important for the overall industrial development of the EU.

The analysis, launch and implementation of the actions contained in this Communication requires that an action plan must be developed and put into place progressively by means of a continued debate between the different actors in the steel business, the Commission and wherever required, experts from the MS. In this respect, the structured dialogue between stakeholders in the steel business, as has been fostered the last 45 years within the ECSC Consultative Committee, has provided a very useful platform for discussions. This especially concerns industrial restructuring, steel markets perspectives, the social dialogue and RTD. The Commission will support the idea of launching, by the business community, of an efficient and flexible forum serving as a platform for a structured dialogue between industrial stakeholders, after the expiry of the ECSC Treaty.

5. CONCLUSION

The Commission considers that the steel industry of the EU, though among the most modern and competitive in the world, faces a set of challenges that must be met in order to maintain and, if possible strengthen further, its international competitiveness. A set of actions, to be developed and pursued by the main stakeholders of the steel business, the Commission and/or Member States, has been identified in the present Communication. The Commission will implement, in co-operation with these actors, a structured follow-up of these actions and it will closely monitor the evolution of the international competitiveness of this sector and it will periodically report to the Council on these issues.

ANNEX 1

Endnotes

¹ COM (98) 718

² The steel industry encompasses, according to the ECSC-definition, steel production from raw material processing to the production of hot finished steel and their derivatives (like tinplate and cold rolled sheet). Flat products such as rolled strip, sheets and plates account for 62% of production volume with the rest mostly going in the form of long products such as rods, bars and heavy sections.

³ Decision 182/1999/EC of the European Parliament and of the Council relating to the 5th Framework Programme of the EC for research, technological development and demonstration activities (1998-2002)

⁴ Statistics over the year 1996, from "The Competitiveness of European Industry", 1998 Report

⁵ Source: The iron and steel workforce of the twenty-first century, ILO, 1997

⁶ According to a study carried out by the "Wirtschaftsvereinigung Stahl" (November 1998).

⁷ COM (1997) 506 "Expiry of the ECSC Treaty : Financial activities" and SEC (1998) 1948, "Working Document" of 16 November 1998

⁸ Council resolutions (98/C/247/04) of 20 July 1998 and (99/C/190/01) of 21 June 1999

⁹ COM (1996) 561 Communication on Environmental Agreements

¹⁰ COM (1998) 259: Social Action Programme 1998 – 2000

¹¹ COM (1998) 322 final "Adapter et promouvoir le dialogue social au niveau communautaire"

¹² See: "The functioning of product and capital markets (Cardiff I)" and "Economic and structural reform in the EU (Cardiff II)", reports presented by the Commission in response to the conclusions of the Cardiff European Council

¹³ See draft Communication from the Commission to the EP and the Council "Assessment of the Single Market Action Plan", January 1999.

¹⁴ Council Regulation (EEC) n° 4064/89

¹⁵ See COM (96) 53: "The Challenge of Global Trade: A Market Access Strategy for the EU".

¹⁶ COM (1998) 463

¹⁷ COM (1998) 220

ANNEX 2

List of abbreviations

AD	Anti Dumping
ASEAN	Association of South East Asian Nations
BAT	Best Available Techniques
BOF	Basic Oxygen Furnace
BREF	BAT Reference Documents
CEEC	Central and Eastern European Countries
CN	Combined Nomenclature (Common Customs Tariff)
CVD	Countervailing Duties
DRI	Direct Reduced Iron
EA	Europe Agreement
EAF	Electric Arc Furnace
EBRD	European Bank for Reconstruction and Development
ECOM-IS	Electronic Commerce Open Marketplace for Industry Sectors
ECSC Treaty	European Coal and Steel Community (Paris, 18 April 1951)
EEC	European Economic Community (Rome, 25 March 1957)
EC Treaty	European Communities (Brussels, 22 January 1972)
EIB	European Investment Bank
HBI	Hot Briquetted Iron
HS	Harmonised System (Common Customs Tariff)
ICT	Information and Communication Technologies
IFC	International Finance Co-operation
IPPC	Integrated Pollution Prevention and Control
MEBF	Mercosur Business Forum
MRA	Mutual Recognition Arrangement
NNSC	Near Net Shape Casting
OECD	Organisation for Economic Co-operation and Development
PHARE	Community programme for economic restructuring in CEEC
RTD	Research and Technological Development
SLIM	Simplified Legislation for the Internal Market
SME	Small and Medium-sized Enterprise
TABD	Transatlantic Business Dialogue
TRIAD	EU, USA and Japan
ULSAB	UltraLight Steel Body
UN	United Nations
UN/ECE	United Nations Economic Commission for Europe
UNFCCC	United Nations Framework Convention on Climate Change
UNCITRAL	United Nations Commission on International Trade Law
WB	World Bank
WTO	World Trade Organisation

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